CONGRESSIONAL BUDGET OFFICE
U.S. CONGRESS
WASHINGTON, D.C. 20515

October 7, 1987

The Honorable William V. Roth, Jr.
Committee on Governmental Affairs
United States Senate
Washington, D.C. 20510

Dear Senator:

As you requested, the Congressional Budget Office has estimated the potential budgetary impact of a bill, identified as the Federal Employees' Optional Early Retirement Act of 1987, as measured against the CBO baseline used in the concurrent budget resolution for fiscal year 1988. During the three-month period starting 60 days after enactment, the bill would allow certain federal civilian employees to retire under relaxed requirements for minimum age and years of service. The bill also would reduce total federal civilian employment to the extent that workers retire, whether under provision of current law or the proposed bill, during the three-month period.

CBO estimates that enactment of the bill would increase direct spending through fiscal year 1992 by some \$2.1 billion. This includes \$1.3 billion in new federal retirement payments and about \$0.8 billion for losses of employee contributions for deferred compensation such as life insurance and retirement benefits. To offset these costs, the bill seeks to curtail the size of the federal civilian work force, and thereby to reduce government payroll expenditures by an estimated \$5.2 billion through 1992. But there is no guarantee that future appropriation levels—and thus budgetary costs—would be reduced accordingly.

Funds for federal employee salaries are appropriated on an annual basis along with funds appropriated for other categories of expenditure. Although the bill is designed to reduce federal employment and lower government spending, Congress may choose a different course of action. The net budgetary effect is contingent upon subsequent actions taken by the Congress.

Payments to Retirees

The bill would increase direct federal spending by an estimated $1.3 billion over the 1988-1992 period for payments to early retirees of their Civil Service Retirement (CSR) benefits and unused annual leave. For those employees who accelerate their retirement, unused leave payments are assumed to average one-month's pay. In addition, about 50 percent of the accelerated group is assumed to elect reductions in future annuity payments in order to receive lump-sum payments that average some $19,000 per person. The possibility of higher administrative costs for processing the surge in new retirements is not considered.

Based on information from the Office of Personnel Management, some 430,000 federal employees would become eligible to draw an immediate CSR pension during the early retirement period. The estimated increase in direct spending assumes that 25 percent of this group will not be given the early retirement option because they are in critical positions, missions, or locations. Costs to the federal government would be higher if the option remains open to all positions. It is difficult to estimate the portion of eligible employees that would decide to retire early if the bill were enacted. Approximately 40 percent of those eligible are age 55 and over. The estimate assumes that 25 percent of this group would take advantage of the retirement option and accelerate their retirement plans. Under current law, most of this group would have retired in 1991 or beyond. The remaining 60 percent of the eligible pool has an average age of 50 with 28 years of federal service. The estimate assumes that 5 percent of the younger group would elect the early retirement benefits, even though the earned annuity is reduced by 2 percent for each year under age 55. In taking the two groups together, we estimate that nearly 10 percent or about 42,000 of the eligible employees would opt for early retirement.

Reductions in Employee Contributions

Reductions in mandatory as well as voluntary employee contributions for deferred benefits programs would accompany individual's decisions to retire early and would increase government costs through 1992 by an estimated $0.8 billion. These include mandatory contributions for CSR and Social Security benefits as well as voluntary contributions for the government-sponsored life insurance program and thrift savings plan.

This estimate is consistent with CBO's February baseline which treats the transactions of the Federal Employees' Thrift Savings Fund as on-budget activities. If these transactions were excluded from budget totals, the bill's direct spending costs through 1992 would change slightly, increasing by less than $0.1 billion. Following the recommendation of the General Accounting Office, CBO's August baseline excludes the transactions of the Thrift Savings Fund from the budget.

Employment Reductions

The President currently exercises broad powers to control the size of the federal civilian work force. They are carried out as part of the budget process and usually entail ceilings on the number of full-time equivalent employees allowed each agency during a given year. Since 1982, the Congress has renewed the yearly prohibition on the use of any "man-year" constraints or limitations in managing the civilian work force at the Department of Defense. By overruling this prohibition, the bill would broaden existing authority to limit the size of the federal work force.

Section 8 of the bill would institute an additional mechanism to reduce the number of federal civilian employees. In particular, it would require the President or his designee to impose a work force ceiling for each agency that declines by the number of employees who retire during the three-months that pension eligibility is relaxed. Although the ceilings would continue for three full years, the President could exempt certain positions determined "essential for the performance of an Executive responsibility." But the maximum number of exemptions for each agency is 10 percent of the vacancies that result from CSR employees retiring during the three-month period ending April 1988.

If no exemptions to government hiring limitations were granted, employment in nonpostal agencies could decline by more than two percent or about 48,000 jobs during the three months ending April 1, 1988. In addition to the employment reduction of 32,000 due to accelerated retirements, some 16,000 other positions would not be filled due to individuals retiring under current CSR old-age and disability provisions. (This assumes that 25 percent of the employees retiring during the three-month period work for the U.S. Postal Service or Postal Rate Commission and therefore their positions could be refilled.) Assuming the Administration grants the maximum number of exemptions and using an average 1988 salary of about $20,000 for each new hire precluded under the bill's provisions, the bill could lower federal payroll levels over the 1988-1992 period by $5.2 billion. (This estimate assumes budgetary resources are not diverted to expanded use of overtime, that managers do not accelerate efforts to use contracting out where financially advantageous, and that agencies will begin to fill the vacancies resulting from the bill's enactment at the end of the hiring limitation period.) However, the realization of any outlay savings remains contingent upon subsequent appropriation actions taken by the Congress.

The possible effect of the bill's employment cutbacks on the level and quality of government services is uncertain, and the cost and magnitude of such impacts cannot be quantified. Even with the 10 percent exemption provision, effective and efficient administration of some defense and nondefense programs could be impaired.

With best wishes,

Sincerely,

Edward Gramlich

Edward M. Gramlich
Acting Director